

**DIVISION OF WATER AND AUDITS**

**Advice Letter Cover Sheet**

**Utility Name:** Del Oro Water Co.

**Date Filed:** 2/22/2019

**[District Name]:** [Hat Creek]

**CPUC Utility #:** WTB 61

**Protest Deadline (20<sup>th</sup> Day):**

**Advice Letter #:** 510

**Review Deadline (30<sup>th</sup> Day):**

**Tier:** 3

**Req. Effective Date:**

**Authorization for Filing:**

**Compliance Filing:**

**Description:** Acquiring water assets & setting up a new DOWC District (Hat Creek) from Hat Creek Water Company.

**Utility Contact:** Janice Hanna

**Alternate:** Bob Fortino

**Phone:** (530) 809-3960

**Phone:** (530) 809-3958

**Email:** [jeh@corporatecenter.us](mailto:jeh@corporatecenter.us)

**Email:** [rsf@corporatecenter.us](mailto:rsf@corporatecenter.us)

**DWA USE ONLY**

Date

Staff

Comments

<u>Date</u>	<u>Staff</u>	<u>Comments</u>
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

ACCEPTED

WITHDRAWN

REJECTED

Signature: \_\_\_\_\_

Comments: \_\_\_\_\_

Date: \_\_\_\_\_

\_\_\_\_\_



February 22, 2019

Advice Letter No. 510

TO THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Del Oro Water Company, Inc. (DOWC) hereby transmits for filing, Advice Letter No. 510 for Commission consideration of DOWC's request to acquire the Hat Creek Water System assets, from the Hat Creek Water Company (Hat Creek), under the terms and conditions set forth in the July 1, 2018 Asset Purchase Agreement between DOWC and Hat Creek **[Exhibit A]**. This proposed transaction is filed pursuant to Public Utilities Code (PU Code) 851-854 which prohibits the sale or transfer of control of a public utility without the advance approval of this Commission.

The following changes in its tariff schedules are attached hereto:

<u>Cal. P.U.C. Sheet No.</u>	<u>Title of Sheet</u>	<u>Schedule No.</u>	<u>Cal. P.U.C. Sheet No.</u>
____-W	Title Page		____-W
____-W	Preliminary Statement		____-W
____-W			____-W
____-W			----
____-W	Service Area Map, Hat Creek District		____-W
____-W	General Metered Service, Hat Creek District	HC-1	----
____-W			----
____-W	Table of Contents		____-W
____-W			____-W
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____-W			____-W



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## **Purpose**

Furthermore, review and approval of DOWC's request for the sale and purchase of Hat Creek may be obtained through the Advice Letter process, since the transaction is valued at less than five million (\$5,000,000); is non-controversial; and does not require environmental review by the Commission as the Lead Agency under the California Environmental Quality Act (CEQA). This process was established in Resolution ALJ-186 and extended and modified by Resolutions ALJ-202, ALJ-244, and ALJ-272.

## **Background**

The Seller desires to sell the water system and Buyer desires to acquire the system as it can be profitably and efficiently consolidated with the regulated water systems Buyer already owns and operates. Buyer has the following experience which qualifies it to operate the subject system. Buyer is a CPUC public utility that has been providing water service to the general public in portions of the State of California since 1963 under the regulatory jurisdiction of the CPUC. Buyer presently serves customers (connections) in ten (10) counties including: 3,319 in Butte County; 405 in Shasta County; 892 in Humboldt County; 384 in Tuolumne County; 90 in Kern County; 56 in Colusa County; 1,032 in Tulare County; 29 in Fresno County; 83 in Glenn County; and 37 in Tehama County

Hat Creek is a class D water utility owned by John Parrish. Hat Creek serves 63 metered customers in the area known as Rim Rock Ranch and vicinity, located in the community of Old Station, Shasta County. The sole water source is surface water out of Hat Creek, for which the utility has diversion rights assigned by the State Water Resources Control Board. All of the water is treated through a filtration system pre- and post-chlorination, plus an injection coagulant. The water is then transported to a 100,000-gallon storage tank (bolted steel) via a 4-inch supply line. A 6-inch (gravity fed) supply line carries the water into the distribution system.



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The water utility will operate as one of DOWC's Districts under the direction of the Regional Superintendent who has been with the company for over 42 years. Under his direction, an Assistant Regional Superintendent (with Del Oro Water for over 32 years), currently stationed near Chico, California, will be responsible for the operation of the new district as well. He is approximately 120 miles from the proposed Hat Creek District. All field personnel are appropriately licensed depending on the operational requirements of the particular system. Hat Creek is approximately 25 miles from DOWC's Johnson Park District located in Burney where there are field personnel.

Central management, including DOWC's 24-hour Call Center, is located at 426 Broadway in Chico, California. All customer service needs, including inquiries and complaints, are directed to central management through an 800 number.

The Hat Creek water system will be acquired by DOWC which will receive a capital contribution for the acquisition by its parent, Utility Management Services, Inc. (UMS). The financial integrity of the acquisition will be upheld by the financial backing of DOWC as well as UMS. The Agreement of Purchase and Sale of Assets is attached as **Exhibit A**.

Hat Creek's last General Rate Case was approved with Resolution W-5161 effective March 22, 2018, establishing their current rates. With the newly established rates, DOWC will not file a general rate case for rates effective sooner than twelve (12) months after the effective date of the purchase.

Included in the Advice Letter 510 package to justify the acquisition are the following exhibits:

**EXHIBIT A** - Agreement of Purchase and Sale of Assets, dated July 1, 2018

**EXHIBIT B** - A Service Area Map of the Hat Creek District of DOWC

**EXHIBIT C** - Resolution W-5161 and Current Rate Structure

**EXHIBIT D** - Fair Market Value by Harold V. Morgan, date June 28, 2018

Del Oro Water Company, Inc.



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**EXHIBIT E** – Proposed Summary of Earnings and Rate Base

**EXHIBIT F** – Notice to Hat Creek Customers to follow.

**File a PROTEST:**

A protest is a document stating that you object to the utility receiving all or some part of its request. If you wish to file a protest, you must state the facts constituting the grounds for the protest, how the advice letter affects you, and the reasons why you believe the whole advice letter, or part of it, is not justified.

If the protest requests an evidentiary hearing (an evidentiary hearing is a legal proceeding held before an administrative law judge at the Commission to obtain evidence), your protest must state the facts you would present at the evidentiary hearing to support your request for a complete or a partial denial of the advice letter. The filing of a protest does not ensure that an evidentiary hearing will be held. The decision whether or not to hold an evidentiary hearing will be based on the contents of the protest.

**File a RESPONSE:**

A response is a document that does not object to the request sought in the application, but nevertheless, presents information you believe would be useful to the Commission in acting on the application.

Whether you wish to file a PROTEST or send a RESPONSE you must:

- Send a copy of your document to the utility
- Mail both one copy to the utility and one copy to CPUC within twenty (20) days of the date you received this notice.

The utility must respond to your protest or response within five (5) days. All protests or responses to this filing should be sent to:

CPUC, Water Division  
505 Van Ness Avenue  
San Francisco, California 94102  
Fax: (415) 703-2481  
E-Mail : [water\\_division@cpuc.ca.gov](mailto:water_division@cpuc.ca.gov)

*and*

DOWC, Director of Community Relations  
Drawer 5172  
Chico, CA 95927  
(530) 717-2500 / Fax: (530) 894-5405  
E-Mail: [communityrelations@delorowater.com](mailto:communityrelations@delorowater.com)





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If you have not received a reply to your protest within ten (10) business days, contact Del Oro Water Company at 1-877-335-6764 or 530-717-2500.

This is a Tier 3 filing. a notice to the customers will be mailed confirming the details of the transaction on Thursday, February 28, 2019. A copy of this notice will be forwarded to the Commission as [Exhibit F].

This filing will not cause withdrawal of service nor conflict with any other schedule or rule.

Del Oro Water Company, Inc.

JANICE HANNA  
Director, Corporate Accounting

Attachment

DRAWER 5172 CHICO, CALIFORNIA 95927 - WWW.DELOROWATER.COM

PARADISE PINES - LIME SADDLE - MAGALIA - STIRLING BLUFFS - FERNDALE - JOHNSON PARK - COUNTRY ESTATES - BLACK BUTTE - CALIFORNIA PINES  
ARBUCKLE - STRAWBERRY - RIVER ISLAND - MT LASSEN - TULARE - METROPOLITAN - TRAVER - BUZZTAIL - LARKSPUR MEADOWS - BENBOW

# TARIFF SCHEDULES

APPLICABLE TO

WATER SERVICE

Together with Information Affecting  
Rates and Service  
of

**DEL ORO WATER CO., INC**

**Drawer 5172  
Chico, CA 95927  
Butte County**

Operating In or Near the Following California Cities and/or Unincorporated Areas

**ARBUCKLE, BAKERSFIELD, BURNEY,  
CALIFORNIA HOT SPRINGS, COLUSA, FERNDALE, FRESNO  
MAGALIA, ORLAND, PARADISE, PORTERVILLE, SHASTA COUNTY, (C)  
SHINGLETOWN, SPRINGVILLE, STIRLING CITY, STRAWBERRY,  
UPPER STILSON CANYON BUTTE COUNTY, and TRAVER**

The effective tariff schedules of this utility, including the rates and rules herein, have been regularly filed with the Public Utilities Commission of the State of California.

No officer, inspector, solicitor, agent or employee of the utility has any authority to waive, alter or amend these tariff schedules or any part thereof in any respect.

To be inserted by utility)

*Issued by*

(To be inserted by Cal. P.U.C.)

Advice Letter No. 510

Date Filed \_\_\_\_\_

Decision No. \_\_\_\_\_

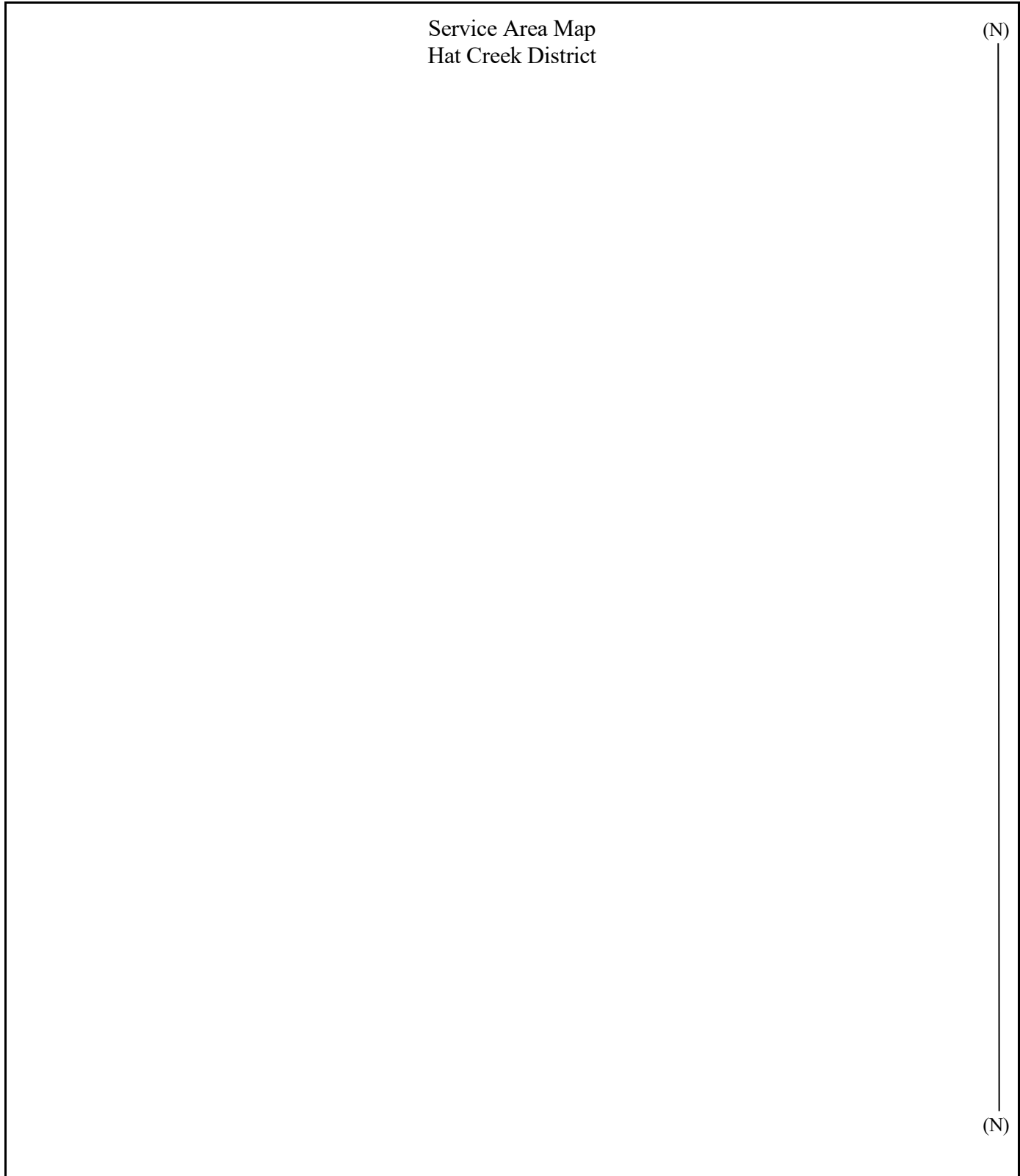
Effective \_\_\_\_\_

**JANICE HANNA**  
Director, Corporate Accounting

Resolution No. \_\_\_\_\_







(To be inserted by utility)  
Advice Letter No. 510  
Decision No. \_\_\_\_\_

*Issued by*  
  
**JANICE HANNA**  
*Director, Corporate Accounting*

(To be inserted by Cal. P.U.C.)  
Date Filed \_\_\_\_\_  
Effective \_\_\_\_\_  
Resolution No. \_\_\_\_\_

Schedule No. HC-1  
GENERAL METERED SERVICE

(N)

HAT CREEK DISTRICT

APPLICABILITY

Applicable to all water service.

TERRITORY

The area known as Rim Rock Ranch, Unit No. 1, and vicinity, located near the community of Old Station, Shasta County.

RATES

Quantity Rate:

	<u>Per Meter</u> <u>Per Month</u>
All usage, per 100 cu. ft. ....	\$ 2.01

Monthly Service Charge:

For 5/8 x 3/4 -inch meter .....	\$33.35
For 3/4 -inch meter .....	52.02
For 1 -inch meter .....	83.36
For 1-1/2 -inch meter .....	166.73
For 2 -inch meter .....	266.76
For 3 -inch meter .....	500.18

The Service Charge is a readiness-to-serve charge, which is applied to all metered service and to which is added the month charge computed at the Quantity Rate.

SPECIAL CONDITIONS

1. The annual service charge applies to service during the 12 month period commencing January 1 and is due in advance. If a permanent resident of the area has been a customer of the utility for at least 12 months, the resident may elect, as the beginning of the calendar year, to pay prorated service charges in advance at intervals of less than one year in accordance with the utility's established billing periods.
2. The established billing cycle for water used is monthly.

(continued)

(N)

(To be inserted by utility)  
Advice Letter No. 510

*Issued by*

(To be inserted by Cal. P.U.C.)  
Date Filed \_\_\_\_\_

Decision No. \_\_\_\_\_

**JANICE HANNA**

Effective \_\_\_\_\_

**Director, Corporate Accounting**

Resolution No. \_\_\_\_\_

(N)

Schedule No. HC-1  
(Continued)

GENERAL METERED SERVICE

HAT CREEK DISTRICT

SPECIAL CONDITIONS (Cont'd.)

- 3. The opening bill for metered service, except upon conversion from flat rate service, shall be established after the first day of any year, the portion of such annual charge applicable to the current year shall be determined by multiplying the annual charge by one three-hundred-sixty-fifth (1/365) of the number of days remaining in the calendar year. The balance of the payment of the initial annual charge shall be credited against the charges for the succeeding annual period. If service is not continued for at least one year after the date of initial service, no refund of the initial annual charges shall be due the customers.
- 4. All bills are subject to reimbursement fee set forth on Schedule No. UF.
- 5. A late charge will be imposed per Schedule No. LC.
- 6. In accordance with Section 2714 of the Public Utilities Code, if a tenant in a rental unit leaves owing the company, service to subsequent tenants in that unit will, at the company's option, be furnished on the account of the landlord or property owner.

(N)

(To be inserted by utility)

Advice Letter No. 510

Decision No. \_\_\_\_\_

*Issued by*

**JANICE HANNA**  
**Director, Corporate Accounting**

(To be inserted by Cal. P.U.C.)

Date Filed \_\_\_\_\_

Effective \_\_\_\_\_

Resolution No. \_\_\_\_\_

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The following listed tariff sheets contain all effective rates and rules affecting the charges and services of the utility, together with other pertinent information.

<b><u>SUBJECT MATTER OF SHEET</u></b>	<b><u>P.U.C. SHEET NO.</u></b>
<b>Title Page</b>	2091-W
<b>Table of Contents</b>	2104-W, 2099-W, 2103-W, 2100-W, 2080-W (C)
<b>Preliminary Statements</b>	
A. Territory Serviced by the Utility	2092-W
B. Types and Classes of Service	2074-W
C. Description of Service	2074-W
D. Procedure to Obtain Service	2074-W
E. Symbols	1683-W
F. CDPH User Fees Balancing Account	1683-W
G. Water Testing Costs Resulting From CDPH Regulations Concerning Water Quality Balancing Account	1684-W
H. Costs Resulting From Catastrophic Events or States of Emergency as Tracked in a Catastrophic Events Memo Acct.	1684-W, 2053-W
I. Cost resulting From Unanticipated Repairs as Tracked in an Unanticipated Repair Costs Memo Account	2053-W
J. PP District Improvement Project Memo Account	2054-W
K. PP, MG, LS District's Extraordinary Memo Account	2054-W, 2055-W
L. LS District 2008 Emergency Water Extraordinary Events Memo Account	2055-W, 2056-W
M. SB District Low Income Ratepayer Assistance Memo Account	2057-W
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O. ST District Purchased Water Memo Account	2058-W, 2059-W
P. DOWC Extraordinary Events Legal/Engineering Memo Account	2059-W
Q. DOWC Transportation Memo Account	2060-W
R. DOWC Extraordinary Events Emergency Water and/or Supplemental Water Memo Account	2060-W
S. RI District Mandatory Conservation Rationing Implementation Memo Account	2061-W
T. RI District Lost Revenue Memo Account	2062-W
U. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 Memorandum Account	2063-W, 2064-W
V. DOWC, Safe Drinking Water State Revolving Fund Loan Repayment Balancing Account (SDWSRF/LRBA)	2064-W
W. DOWC Statewide Lost Revenue Recovery Memorandum Account (SLRRMA)	2065-W

(To be inserted by utility)

Issued By

(To be inserted by P.U.C.)

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Date Filed \_\_\_\_\_

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**Director, Corporate Accounting**

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**Rate Schedules (cont.):**

**Country Estates District**

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**Ferndale District**

Schedule No. FD-1A, Annual General Metered Service 1648-W, 1649-W, 1933-W

Schedule No. FD-4, Private Fire Protection Service 407-W, 408-W

**Hat Creek District**

Schedule No. HC-1, General Metered Service \_\_\_\_-W (N)

**Johnson Park District**

Schedule No. JP-1A, Annual General Metered Service 1900-W, 1974-W

Schedule No. JP-F, Facilities Fees 902-W

**Lime Saddle District**

Schedule No. LS-1A, Annual Metered Service 1666-W, 1958-W, 1358-W,  
1413-W, 2177-W,

Schedule No. LS-F, Facilities Fee 2178-W

**Magalia District**

Schedule No. MD-1A, General Metered Service 2134-W, 2036-W, 2170-W

**Metropolitan District**

Schedule No. MP-1, General Metered Service 2024-W, 2017-W

**Mt. Lassen District**

Schedule No. ML-1A, Annual General Metered Service 830-W, 831-W

Schedule No. ML-2A, Monthly Stand-By Rate Flat Rate Service 832-W, 833-W

Schedule No. ML-MHF, Meter Hook-Up Fee 845-W

**Paradise Pines District**

Schedule No. PP-1A, Annual General Metered Service 2147-W, 1446-W, 2171-W,

Schedule No. 14.1, Water Shortage Contingency Plan with  
Staged Mandatory Reduction and Drought  
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1769-W, 1770-W

(To be inserted by utility)

Issued By

(To be inserted by P.U.C.)

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**SUBJECT MATTER OF SHEET**

**P.U.C. SHEET NO.**

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<b>Table of Contents</b>	___-W, (C)
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	2099-W,
	2103-W,
	2126-W,
	2011-W

(To be inserted by utility)

*Issued By*

(To be inserted by P.U.C.)

Advice Letter No. 510

***Janice Hanna***

Date Filed \_\_\_\_\_

Decision No. \_\_\_\_\_

***Director, Corporate Accounting***

Effective \_\_\_\_\_

Resolution No. \_\_\_\_\_

## **Exhibit B**

**Del Oro Water Company  
Hat Creek District  
Advice Letter No. 510**

**Service Area Map**



## **Exhibit C**

**Del Oro Water Company  
Hat Creek District  
Advice Letter No. 510**

**Resolution W-5161 and  
Current Rate Structure**

**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

**WATER DIVISION**

**RESOLUTION W-5161**

**March 22, 2018**

**RESOLUTION**

**(RES. W-5161) HAT CREEK WATER COMPANY. ORDER  
AUTHORIZING A GENERAL RATE INCREASE TO  
PRODUCE ADDITIONAL ANNUAL REVENUES OF  
\$18,621, OR 52.9%, FOR TEST YEAR 2018, TO BE PAID BY  
THE RATEPAYERS.**

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**SUMMARY**

By Advice Letter 30-W, filed on November 15, 2017, Hat Creek Water Company seeks to increase its gross annual revenues by \$17,266, or 49.1%, for Test Year 2018. Hat Creek Water Company's rate increase request is based upon an increase in operating expenses.

For Test Year 2018, this resolution grants Hat Creek Water Company an increase in gross annual revenues of \$18,621, or 52.9%, which is estimated to provide total annual revenues of \$53,800 based on a Rate of Margin (ROM) of 23.87%. The monthly bill for an average customer with a 5/8 x 3/4-inch metered residential customer using 10 CCF per month would increase from \$33.07 to \$53.43, or 61.6%.

**BACKGROUND**

Hat Creek Water Company (Hat Creek) is a Class D water utility that has requested authority under General Order 96-B, General Rule 7.6.2, Water Industry Rule 7.3.3(5), and Public Utilities Code Section No. 454 to increase its water rates by \$17,266 or 49.1%, for Test Year (TY) 2018.

The last general rate increase (GRC) was granted on May 7, 2015, pursuant to Resolution (Res.) W-5020, which authorized a rate increase of \$15,561, or 71.0%, resulting in a Rate of Margin of 21.69% for TY 2015. The present rates became effective on August 31, 2017, pursuant to the approval of Advice Letter (AL) 29-W, which granted a Consumer Price Index (CPI) increase of 2.1%.

Hat Creek is a class D water utility owned by John Parrish, who provides overall management, engineering, and maintenance services. Mr. Parrish is a Grade D1 Water Distribution Operator and a Grade T2 Water Treatment Operator. In addition to providing technical operations for the utility, Mr. Parrish is responsible for accounts receivable, billings, banking, bookkeeping, and customer relations. Hat Creek serves 63 metered customers in the area known as Rim Rock Ranch and vicinity, located in the community of Old Station, Shasta County. A total of 53 customers have 5/8" x 3/4" meters.

The sole water source is surface water out of Hat Creek, for which the utility has diversion rights assigned by the State Water Resources Control Board. All of the water is treated through a filtration system pre and post-chlorination, plus an injection coagulant. The water is then transported to a 100,000 gallon storage tank (bolted steel) via a 4-inch supply line 1,800 feet to the storage tank. A 6-inch (gravity fed) supply line carries the water into the distribution system.

There are four 1-inch customers, which include the Forest Service Camp Ground, the Forest Service Visitor Center, the Cascade Showers/laundry mat facility, and the fourth being a resident. The 1-1/2-inch meter serves the Rim Rock Ranch Resort, which closes during the winter. The two 2-inch meters serve the Forest Service Work Center and the Forest Service Camp Ground, which is, per agreement, charged at the 1-inch meter charge. Lastly, the 3-inch meter is provided for Cal-Trans. The number of customers is not expected to change in the upcoming years, so Hat Creek estimates no additional customers for TY 2018.

## **NOTICE AND PROTESTS**

A notice of the proposed rate increase was mailed to all customers. In this public notice, all customers were informed of the 49.1% increase in revenues and the new rates. A copy of the notice was mailed to each customer on January 6, 2018. No protests or comments have been received.

## **DISCUSSION**

The Water Division (Division) made an independent analysis of Hat Creek's rate increase request. Appendix A shows Hat Creek's and the Division's estimates of the summary of earnings at present, requested, and recommended rates. Division is in concurrence with Hat Creek's estimates in operating revenues, expenses, and rate base.



Division reviewed operating revenues and expenses including employee labor, materials, contract work, water testing, transportation expenses, other plant maintenance, office salaries, office supplies and expenses, insurance, general expenses, depreciation, and taxes other than income. Division verified the operating expenses by reviewing supporting documents for substantiation and accuracy, and included the amounts that were deemed reasonable and prudent. The ratebase and the adopted quantities contained in Appendix D are also updated to reflect TY 2018.

**Operating Revenues**

Hat Creek’s operating revenues consist of general metered sales. There are currently 63 active service connections. For the TY, Hat Creek does not expect to add or lose any customers. A review of the past recorded numbers of customers during the past five years indicates there has been essentially no change in the number of customers, therefore, Division concurs with the utility’s estimate of customers and revenues at present rates.

**Operating Expenses**

Hat Creek and the Division concur with the estimates for operating expenses based upon the recorded operating expenses from the 2014, 2015, and 2016 annual reports. Hat Creek applied a three-year average, and then applied the appropriate labor and non-labor inflation rates to each category for 2017 and TY 2018. In the previous GRC, and in the adopted summary of earnings in Resolution W-5020, Hat Creek neither requested, nor estimated, expenses for any of the following:

	<u>Adopted 2015</u>	<u>TY-2018</u>
• Other volume related expenses	\$0	\$2,906
• Employee labor	\$0	\$3,900
• Water testing	\$0	\$1,948
• Office salaries	\$0	\$1,455
• Employee benefits	\$0	\$1,900
• Uncollectibles expense	\$0	\$12

However, in its AL 30 and its supporting workpapers, Hat Creek applied the appropriate amounts recorded in its annual reports and estimated using the forecasting methods discussed above.

Hat Creek has received grants, principally for a new treatment system, that have resulted in significant improvements for the water system. While the plant facilities are in good condition, they are mostly contributed or fully depreciated plant. For quite some time, and in an effort to keep rates low in the community, Mr. Parish has elected to forgo management salaries, employee labor, and other expense items commonly associated in operating expenses for Class D water utilities in similar scope and size. In addition, Mr. Parish is nearing retirement, and the successor and/or future manager or owner will need to both be compensated and meet such reasonable operating expenses accordingly.

As a result, this arrangement has kept net revenues low; however, this business model is not sustainable, and it has come to the point where Hat Creek should record expenses in these accounts, especially if Mr. Parish retires and/or hires an operator to assist in system operation. The Division finds it reasonable that the modest amounts proposed for employee labor, office salaries, and employee benefits are fully warranted.

Prior to 2016, and in the previous GRC, Other Volume Related expenses (USOA 618) were embedded into the General Expenses category. Similarly, Water Testing expenses were embedded into Contract Work – Others (USOA 650). Beginning in 2016, with the assistance of an accounting consultant, both Other Volume Related and Water Testing expenses were reallocated accordingly into their appropriate line items.

Uncollectibles, monies not received or shortfalls, were relatively low and were recorded as zero in both the 2014 and 2015 annual reports. Beginning in 2016, with the assistance of an accounting consultant, Hat Creek was advised to record \$35 in unaccounted for revenues. Using the forecasting method described above, Hat Creek took a three year average (2014 through 2016), and escalated accordingly to estimate Uncollectibles for TY 2018.

### **Plant Additions and Ratebase**

There have been no additions to plant or ratebase since the previous GRC.

### **Rate of Return vs. Rate of Margin**

Hat Creek has requested a ROM of 23.87%. Two methods are available for the Division to utilize in the rate-making process: (1) ROR and (2) ROM. In Res. W-4524 (March 17, 2005), the Commission adopted a revised set of standard practices for determining the profit for Class C and D water utilities using the rate of return and rate of margin

methods. Both methods are to be used. Per Decision 92-03-093, dated March 31, 1992, Division must recommend the method that produces the higher revenues. In the ROM method, the utility's revenue requirement is defined as the sum of its operating and maintenance expenses, depreciation, income and other taxes, multiplied by the ROM. This method gives the small water utilities the opportunity to earn a more reasonable and appropriate revenue requirement when the utility has "little rate base". If only the ROR method was used, a utility with little or no ratebase would earn little or no return. The Division recommended ROR is 10.50% to 11.50% for a Class D, 100% equity-financed utility. Division has recommended a ROM of 23.87% for Class D water utilities.<sup>1</sup> Applying a ROR of 11.50% yields a net income of \$334 versus a \$10,368 when applying a ROM. This comparison of the two methods indicates that the ROM method produces a higher revenue requirement; therefore, Division recommends the ROM method at 23.87%.

#### Taxes

Due to changes in the Federal tax rates, Division applied a 21% flat tax rate. In its filing, Hat Creek applied a 15% Federal tax rate to the first \$50,000 of income. Accordingly, the Federal income tax expense increased from \$1,783 to \$2,756 for Test Year 2018.

#### Comparison of Water Bills

Class D utilities are authorized by Decision 92-03-093 to request to recover *up to* 100% of fixed costs in the service charge. Hat Creek requested this rate structure in its filing, and the Division concurs. Hat Creek's present rate structure consists of one schedule: Nos. 1 – General Metered Service. The rates proposed by the Division are shown in Appendix B. At Division's recommended rates shown in Appendix B, the monthly bill for an average customer with a 5/8 x 3/4-inch metered residential customer using 10 CCF per month would increase from \$33.07 to \$53.43, or 61.6%. A comparison of customer bills at present and recommended rates is shown in Appendix C. The Adopted Quantities and Tax Calculations are shown in Appendix D.

#### Affordability of Proposed Rates

At Division's recommended rates shown in Appendix B, the average bill for a 5/8 x 3/4-inch metered residential customer consuming 10 CCF per month would increase from

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<sup>1</sup> Water Division Memorandum entitled "Rates of Return and Rates of Margin for Class C and Class D Water Utilities" dated February 4, 2017

\$33.07 to \$53.43, or 61.6% in TY 2018. Hat Creek Water Company is located in the 96071 zip code in Shasta County, near the town of Old Station, where the annual median household incomes (MHI), respectively for the zip code, county and town are \$37,061, \$36,791 and \$45,582<sup>2</sup> The proposed rate, accordingly, would be 1.74%, 1.75% and 1.41% of the respective MHIs.

It should be noted that no affordability criteria has been developed and adopted in any Commission Decision or Resolution. However, in October 2017, the Health and Safety Code in the California Code of Regulations (Sec. 116760.50) was amended to establish an affordability threshold of 1.5% of MHI for average water bills in Severely Disadvantaged Communities, as defined (60% of California Statewide MHI of \$60,818, or \$37,091)<sup>3</sup>. While the Commission adheres to cost-of-service regulatory principles in developing rates for its jurisdictional utilities, and the Division's recommended rates for Hat Creek Water are a minimum to satisfy the utility's technical, managerial and financial capacity and operational capability, the discussion regarding affordability is presented, nonetheless, to indicate to the Commission the relationship between the proposed rates and local economic circumstances.

### **Balancing Accounts**

Hat Creek currently has no pending or outstanding balancing accounts.

### **SAFETY**

Hat Creek meets all applicable drinking water quality standards as required by the State Water Resources Control Board, Division of Drinking Water (SWRCB).

There are no fire districts within the service area and Hat Creek has provided Division with the locations and technical specifications of the five hydrants throughout the service area. Hydrants are flushed once annually and inspected during the fall season to ensure they are drained appropriately to prevent freezing.

The water treatment plant is monitored on a daily basis, either by remote computer or manually. Since this is a one-person operation, the level of safety is a high priority for the utility owner.

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<sup>2</sup> Income by Zip Code - California - 96071

<sup>3</sup> See Assembly Bill 560 (Salas); Chaptered by Secretary of State on October 7, 2017 - Chapter 552, Statutes of 2017.

**COMPLIANCE**

Hat Creek has no outstanding compliance orders and has been filing annual reports as required. Hat Creek meets all applicable drinking water quality standards as required by the SWRCB.

**COMMENTS**

This is an uncontested matter that pertains solely to a water corporation. Accordingly, pursuant to Public Utilities Code Section 311(g)(3), this resolution is exempt from the 30-day period for public review and comment.

**FINDINGS**

1. The Summary of Earnings (Appendix A) recommended by the Water Division (Division) is reasonable and should be adopted.
2. The rates recommended by the Division (Appendix B) are reasonable and should be adopted.
3. The quantities (Appendix D) used to develop the recommendations of the Division are reasonable and should be adopted.
4. The water rate increase authorized herein is justified and the resulting rates are just and reasonable.
5. Hat Creek Water Company should be allowed to file a Tier 1 advice letter to supplement to Advice Letter No. 30 to incorporate the rate schedules (Appendix B), and to concurrently cancel its presently effective Rate Schedules. The effective date of the revised rate schedule should be 5 days after the date of filing.
6. This is an uncontested matter subject to the public notice comment exclusion provided in the PU Code Section 311(g)(3).

**THEREFORE, IT IS ORDERED THAT:**

1. Authority is granted under Public Utilities Code, Section 454, for Hat Creek Water Company to file a supplement to Advice Letter No. 30 to incorporate the rate schedules (Appendix B), and to concurrently cancel its presently effective Rate Schedules. The effective date of the revised rate schedule shall be 5 days after the date of filing. This advice letter shall become effective upon approval by Staff of the Division of Water and Audits.
2. Hat Creek Water Company is authorized to increase the Test Year 2018 water revenues by \$18,621 or 52.9%.

This resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed, and adopted at a conference of the Public Utilities Commission of the State of California held on March 22, 2018; the following Commissioners voting favorably thereon:

/s/ ALICE STEBBINS

ALICE STEBBINS  
Executive Director

MICHAEL PICKER  
President

CARLA J. PETERMAN

LIANE M. RANDOLPH

MARTHA GUZMAN ACEVES

CLIFFORD RECHTSCHAFFEN

Commissioners



**APPENDIX A**  
**HAT CREEK WATER COMPANY**  
**Summary of Earnings – Test Year 2018**

	Utility Estimated Rates		Division Rates	Recommended Rates
	Present	Requested	Present	
<b><u>Operating Revenue</u></b>				
General Metered Revenue	\$35,179	\$52,445	\$53,800	\$53,800
General Unmetered Revenue	\$0	\$0	\$0	\$0
Reclaimed Water Sales	\$0	\$0	\$0	\$0
Private Fire	\$0	\$0	\$0	\$0
Other Water Revenue	\$0	\$0	\$0	\$0
Other Unmetered Revenue	\$0	\$0	\$0	\$0
<b>Total Revenue</b>	<b>\$35,179</b>	<b>\$52,445</b>	<b>\$53,800</b>	<b>\$53,800</b>
<b><u>Operating Expenses</u></b>				
610 Purchased Water	\$0	\$2,245	\$0	\$2,245
615 Purchased Power	\$3,044	\$2,816	\$3,044	\$2,816
618 Other Volume Related Expenses	\$0	\$2,906	\$0	\$2,906
630 Employee Labor	\$0	\$3,900	\$0	\$3,900
(Labor Capitalized)	\$0	\$0	\$0	\$0
640 Materials	\$3,133	\$2,001	\$3,133	\$2,001
650 Contract Work	\$4,343	\$1,603	\$4,343	\$1,603
Water Testing	\$0	\$1,948	\$0	\$1,948
660 Transportation Expenses	\$950	\$1,028	\$950	\$1,028
664 Other Plant Maintenance	\$1,977	\$2,348	\$1,977	\$2,348
670 Office Salaries	\$0	\$1,455	\$0	\$1,455
671 Management Salaries	\$4,800	\$4,989	\$4,800	\$4,989
674 Employee Benefits	\$0	\$1,900	\$0	\$1,900
676 Uncollectibles Expense	\$0	\$12	\$0	\$12
678 Office Services & Rentals	\$0	\$0	\$0	\$0
681 Office Supplies & Expenses	\$2,740	\$2,489	\$2,740	\$2,489
682 Professional Services	\$255	\$892	\$255	\$892
684 Insurance	\$2,600	\$2,646	\$2,600	\$2,646
688 Regulatory Commission Expense	\$0	\$131	\$0	\$131
689 General Expenses	\$5,262	\$3,887	\$5,262	\$3,887
<b>Total Expenses</b>	<b>\$29,104</b>	<b>\$39,195</b>	<b>\$29,104</b>	<b>\$39,195</b>
Depreciation	\$0	\$0	\$0	\$0
Taxes other than Income	\$669	\$208	\$669	\$208
State Income Tax	\$800	\$1,153	\$800	\$1,273
Federal Income Tax	\$0	\$1,783	\$0	\$2,756
<b>Total Deductions</b>	<b>\$30,573</b>	<b>\$42,339</b>	<b>\$30,573</b>	<b>\$43,432</b>
<b>Net Revenue</b>	<b>\$4,606</b>	<b>\$10,106</b>	<b>\$4,606</b>	<b>\$10,368</b>
<b>RATE BASE</b>				
Utility Plant	\$955,815	\$953,365	\$955,815	\$953,365
Construction Work in Progress	\$0	\$0	\$0	\$0
Materials and Supplies	\$1,029	\$2,001	\$1,029	\$2,001
Working Cash	\$2,409	\$3,266	\$2,409	\$3,266
Accumulated Depreciation	\$955,815	\$955,815	\$955,815	\$955,815
Advances for Construction	\$0	\$0	\$0	\$0
Contributions in Aid of Construction	\$0	\$0	\$0	\$0
Deferred Income Taxes	\$0	\$0	\$0	\$0
<b>TOTAL RATE BASE</b>	<b>\$3,438</b>	<b>\$3,266</b>	<b>\$3,438</b>	<b>\$3,266</b>
<b>Rate of Margin (ROM)</b>				<b>23.87%</b>

END OF APPENDIX A

**APPENDIX B**  
**HAT CREEK WATER COMPANY**

Schedule No. 1  
GENERAL METERED SERVICE

APPLICABILITY

Applicable to all metered water service.

TERRITORY

The area known as Rim Rock Ranch, Unit No. 1, and vicinity, located near the community of Old Station, Shasta County.

RATES

Quantity Rate:

All Water used per 100 cu.ft	\$2.01	(I)
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Service Charge:

Per Meter Per Month

For	5/8 x 3/4 inch meter	\$ 33.35	(I)
For	3/4-inch meter	\$ 52.02	(I)
For	1-inch meter	\$ 83.36	(I)
For	1-1/2-inch meter	\$166.73	(I)
For	2-inch meter	\$266.76	(I)
For	3-inch meter	\$500.18	(I)

The Service Charge is a readiness-to-serve charge which is applicable to metered service and to which is to be added monthly charge computed at the Quantity Rate.

SPECIAL CONDITIONS

1. In the event that a customer terminates service under this schedule and reinstates service at the same location, there will be a reconnection charge equal to the minimum charge which would have been billed had the customer not terminated service.
2. All bills are subject to the reimbursement fee set forth on Schedule No. UF

**END OF APPENDIX B**

**APPENDIX C**  
**HAT CREEK WATER COMPANY**

Comparison of Rates  
Test Year 2018

METERED SERVICE	Per Service Connection Per Month		
	Present <u>Rates</u>	Proposed <u>Rates</u>	Percent <u>Increase</u>
Service Charge:			
For 5/8 x 3/4 - inch meter	\$21.47	\$33.35	55.3%
Quantity Charge:			
All water, per 100 cu. ft.	\$1.16	\$2.01	73.2%

Comparison of a monthly typical bill for residential metered customers with a 5/8 x 3/4 - inch meter is shown below at current rates and recommended rates for Test Year 2014.

Usage 100 cu. ft.	Present Rates	Recommended Rates	Percent of Increase
0	\$21.47	\$33.35	55.3%
5	27.27	43.39	59.1%
10 (avg.)	33.07	53.43	61.6%
15	38.87	63.48	63.3%
20	48.15	73.52	52.7%
30	56.27	96.61	66.4%

**END OF APPENDIX C**

**APPENDIX D (Page 1/2)**  
**HAT CREEK WATER COMPANY**  
ADOPTED QUANTITIES  
Test Year 2018

Expenses:

1. Purchased power (Electric)

Total cost (\$)	\$2,816
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2. Purchased Water \$2,245

3. Insurance Expense \$2,646

4. Number of Service Connections:

Metered Rate

5/8 x 3/4 inch meter	54
3/4-inch meter	0
1-inch meter	6
1-1/2 inch meter	1
2-inch meter	1
3-inch meter	<u>1</u>

Total	<u>63</u>
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5. Total Water Sales-Metered Customers 11,116 Ccf

**(cont.)**

**APPENDIX D (Page 2/2)**  
**HAT CREEK WATER COMPANY**  
ADOPTED QUANTITIES  
Test Year 2018

Line No.	Item	State Tax	Federal Tax
1.	Operating Revenue	\$53,800	\$53,800
2.	O & M Expenses	\$39,195	\$39,195
3.	Taxes Other Than Income	\$ 208	\$ 208
4.	Depreciation and Interest	\$ 0	\$ 0
5.	Taxable Income for State Tax	\$14,397	
6.	State Tax	\$1,273	
7.	Taxable Income for FIT		\$13,124
8.	Federal Income Tax		\$2,756
9.	Total Income Tax		\$4,029
	California Corporate Franchise Rate	8.84%	
	Federal Income Tax Rate Flat Rate	21%	

**END OF APPENDIX D**

**HAT CREEK WATER COMPANY  
ADVICE LETTER NO. 30  
SERVICE LIST**

Board of Supervisors  
1415 Court St., Suite 308B  
Redding, CA 96001-1673

Jack Hawks, Director  
CWA  
601 Van Ness Ave., Ste. 2047  
San Francisco, CA 94102  
[jhawks@calwaterassn.com](mailto:jhawks@calwaterassn.com)

Big Springs Mutual Water Co.  
P.O. Box 132  
Old Station, CA 96071  
[Hatcrk49@citilink.net](mailto:Hatcrk49@citilink.net)

Hat Creek Highlands Mutual  
Water Co.  
P.O. Box 62  
Old Station, CA 96071  
[jandismmons@frontiernet.net](mailto:jandismmons@frontiernet.net)

CDDW  
364 Knollcrest Dr., Suite 101  
Redding, CA 96002  
[mikemcnamara@cdph.ca.gov](mailto:mikemcnamara@cdph.ca.gov)

**Exhibit C  
Del Oro Water Company  
Hat Creek District  
Current Rates  
Test Year 2019**

	Customers	Total Bills	Present Rates	Revenue
5/8x3/4"	54	648	<b>33.35</b>	21,611
3/4"	0	0	<b>52.02</b>	0
1"	6	72	<b>83.36</b>	6,002
1.5"	1	12	<b>166.73</b>	2,001
2"	1	12	<b>266.76</b>	3,201
3"	1	12	<b>500.18</b>	6,002
	<hr style="width: 50%; margin: 0 auto;"/>			<hr style="width: 50%; margin: 0 auto;"/>
	63			38,817
Adopted Quantities (ccf)		7,455	<b>2.010</b>	<hr style="width: 50%; margin: 0 auto;"/>
				14,985
				<hr style="width: 50%; margin: 0 auto;"/>
				53,801

**Bill Comparison - 3/4" service  
Metered Customers**

Usage (ccf)	Present Rates	
0	33.35	
<span style="border: 1px solid black; padding: 2px;">10</span>	<span style="border: 1px solid black; padding: 2px;">53.45</span>	Average Bill per Resolution W-5161
20	73.55	
30	93.65	
40	132.42	

## **Exhibit D**

**Del Oro Water Company  
Hat Creek District  
Advice Letter No. 510**

**Harold V. Morgan June 28, 2018  
Fair Market Value**



*Harold V. Morgan*  
CIVIL ENGINEER

*Utility Consulting*  
WATER SYSTEMS  
WASTEWATER SYSTEMS  
WATER RIGHTS

20726 BLACKHAWK STREET  
CHATSWORTH, CALIFORNIA 91311  
~~(818) 552-6435~~  
(818) 388-1746 CELL  
hvmorgan@sbcglobal.net

**CONFIDENTIAL**

June 28, 2018

Mr. Robert Fortino, President  
Del Oro Water Company  
426 Broadway Avenue, Suite 301  
Chico, California 95928

**Subject: A Preliminary Opinion of Fair Market Value of Hat Creek Water Company**

Dear Mr. Fortino:

In accordance with the agreement between Del Oro Water Company (DOWC) and myself, I have made a review and analysis of data supporting a preliminary opinion of fair market value of the water utility known as Hat Creek Water Company (HCWC). This report expresses an opinion of fair market value as of December 31, 2017. I have also made a field visit associated with this appraisal study to review the condition of above-ground water system facilities and the characteristics of the service area. It is my understanding that this valuation analysis may be used by DOWC to negotiate for the purchase of the system.

As used in this letter, fair market value is defined as the highest price in terms of money which a water system would bring if exposed for sale on the open market, by a seller who is willing but not under compulsion to sell, with a reasonable time allowed to find a buyer who is willing but not obligated to buy, with both parties having full knowledge of the uses, purposes and limitations of the property involved. Based upon my investigation of HCWC, it is my preliminary opinion that the fair market value of this system, as of December 31, 2017, is \$80,000. The following sections discuss in greater detail the basis for this opinion.

The opinion of value assumes the acquisition of the utility plant assets, easements, business franchise rights, going concern value, goodwill, and materials and supplies. However, the opinion does not include working funds, current and accrued assets, deferred debits, or other investment and fund accounts of HCWC. Further, no debts, current and accrued liabilities, deferred credits or reserves are envisioned to be assumed by the purchaser. In summary, it is the assets and operating rights of HCWC used in its water system operations, and not related current assets or liabilities of the company that would be transferred in a sale.

#### **DATE OF VALUE**

The opinion of fair market value expressed in this letter is based upon a date of valuation of December 31, 2017, i.e., the facilities and intangible assets being valued are those which existed as of December 31, 2017. This date was chosen because of the availability of recent financial statements plus regulatory records. It is believed that the accounting balances of the system assets as of the date of this report would not be significantly different than the balances expressed in the Company's PUC annual report as of December 31, 2017. Any necessary adjustments to account for financial changes since the end of 2017 would be made at the time of finalizing this preliminary opinion of value.

#### **SCOPE OF INVESTIGATION**

Studies and preparation undertaken in connection with this appraisal include the following:

1. A field visit to view selected above-ground facilities comprising the utility plant and to review the characteristics of the service area. This visit was made with assistance from the company's owner, Mr. John Parrish.
2. Interview of the company's owner, Mr. John Parrish, during the field visit to investigate system operations and facilities, construction materials, water quality issues, system design and historic development, leak and

water losses, ratepayer characteristics and satisfaction, potential service area growth, plans and needs for system improvements. Mr. Parrish also provided copies of water quality tests, service area maps, facility inventories and other records.

3. Review of selected historic accounting records (from December 31, 2000 through December 31, 2017) representing annual plant asset additions and related annual depreciation, as presented in annual reports to the California Public Utilities Commission (PUC); plus the most recent rate case resolutions (W-5020 and W-5161) dated May 7, 2015 and March 22, 2018, respectively. Also reviewed was the financial audit of the company for years 2014 and 2015 conducted by the PUC.
4. Review of State Water Resources Control Board, Division of Drinking Water (SWRCB) annual inspection report dated September 18, 2017; water supply permit; recent ratepayer water quality consumer reports; annual reports filed by the company to the SWRCB for 2014, 2015 and 2016; and other records. This review also included an office discussion with Ms. Mey Bunte, representative responsible for regulatory oversight. An inspection report by the Shasta County Resource Management Department for the system dated July 12, 2011 was also reviewed (regulatory oversight was transferred from the County to the SWRCB in December 2013).
5. A reconnaissance review of decreed and licensed water rights for HCWC as presented in state licensee reports.
6. Water quality and filter plant operating test results based on data supplied by John Parrish and the SWRCB.
7. Estimation of the anticipated rate base that would be expected to be allowed by the PUC following a sale in determining the amount of investment returns which would be allowed on these facilities under private ownership by a Class B (2,000 to 10,000 connections) utility.

8. Performance of a capitalization of earnings study for a purchaser under PUC regulation based on an anticipated market return to an escalated rate base.
9. Consideration of an alternative capitalization of earnings study based on an anticipated PUC authorized gross operating margin allowed to a Class C (500 to 2,000 connections) or D (less than 500 connections) water utility buyer.
10. Investigation of sales of those systems identified to be comparable to this system. However, on account of the minimal rate base existing for this utility and the absence of comparable small system sales in recent years, this approach was not utilized.
11. Consideration of a reproduction cost new less depreciation (RCNLD) analysis for the water system assets based on recent annual report additions for grant funded facilities, historic pipeline inventories and experience gained by me in preparing many RCNLD studies of similar properties.

### QUALIFYING CONDITIONS

The opinion of value expressed in this letter is subject to the following qualifying conditions:

1. The valuation assumes good and clear title to the property and facilities being valued.
2. The appraisal assumes a prospective sale of the utility property would occur on an all-cash basis.
3. The subject of this appraisal is the water system assets associated with the HCWC system including operating rights and obligations, going concern value and service area franchise. Included are all assets used in the operation of the system including reservoir, water treatment plant, transmission and distribution pipelines, land, pumping equipment,



meters, services, hydrants, other equipment and, materials and supplies. However, not included in the opinion of value are working funds, current and accrued assets, deferred debits, or other investment and fund accounts of HCWC (if any).

4. The valuation assumes that no debt obligations attached to the system would be assumed by the purchaser. That is, no debts, current and accrued liabilities, deferred credits or reserves are envisioned to be assumed. Customer deposits are assumed to be refunded to ratepayers before transfer.
5. The facilities included in the appraisal are considered to have been dedicated to public use, and their use by a purchaser (other than a public agency or mutual users organization) would be under the regulatory jurisdiction of the California PUC. It is also assumed that a purchaser; would be able to obtain a permit from the SWRCB in order to operate the water system.
6. The information and data reported in connection with this appraisal have been obtained from sources which are deemed reliable and, after review, are believed to be substantially correct.
7. The appraiser has no present or prospective direct or indirect financial interest connected with any of the parties involved with this utility, and his employment in preparing this appraisal report is not in any manner contingent on finding of any specified or implied values, or otherwise contingent on anything other than the preparation of this opinion.
8. The preliminary opinion of fair market value expressed in this report may be updated after further analysis of: additions or deletions of assets from those contemplated for potential sale as represented in this report; records and documents subsequently produced by HCWC; further review or performance of studies undertaken generally described in the above section on scope of investigation; subsequent comparable water company sales discovered or occurring after the date of this report; documents produced as a result of future regulatory proceedings regarding this system; additional reports, facts or conclusions developed as a result of

studies made on the water system facilities; results of studies performed by other experts pertaining to this system either subsequently made or produced by the parties to this transaction; and additional studies deemed necessary by the appraiser as a result of any of the above in order to refine this opinion. It is also contemplated that a change in the date of value may result in a change in the opinion of value.

9. The opinion of value reached in this report is at this time preliminary. Accordingly, I have made no due diligence investigations, and make no representations regarding the adequacy of HCWC regulatory compliance, status of water rights, land titles and easements, system condition and related matters which might affect future operations or impact the ability of the system to generate anticipated incomes envisioned by this appraisal analysis. Additionally, if any due diligence studies conducted by the buyer reveal defects not considered in this report, adjustments to the appraisal opinion of value may be warranted.

### **METHODS OF APPRAISAL**

The methods of valuation considered in the development of the opinion of fair market value of HCWC system assets included capitalization of earnings (income approach) and reproduction cost new less depreciation or RCNLD (cost approach). A comparable sales (market approach) analysis of the system was considered, but not conducted for the reasons stated below.

### **DESCRIPTION OF SYSTEM**

The HCWC serves approximately 57 residential and 6 commercial customers (including a gas station, restaurant, laundry facility, Caltrans work center, and several USFS locations) in a service area located in the community of Old Station, Shasta County, California. The system was originally constructed in 1960 to serve the Rim Rock subdivision. Distribution extensions were made in 1970 and the early 1980s. This original plant includes approximately 4,826 feet

of 3-inch and 4-inch transite asbestos cement installed in 1960 with an additional 5,691 feet of 2-inch to 4-inch schedule 40 polyvinyl chloride pipe added in the 1970 to 1983 period. Recently, in 2014 and 2015 the utility was awarded up to a \$1 million grant to construct a new surface water treatment plant, a 100,000 gallon storage reservoir and associated facilities. An amount of about \$929,000 was expended to complete the construction. All users are metered. A field visit was made to the system observing the new treatment plant, intake conveyance and service area. Potential growth is very limited with some unbuilt lots and the small possibility of new connections through service area extensions.

New metered rates have recently been approved by the PUC (March 2018). A ratepayer using an average amount of 1000 cubic feet monthly will now pay \$53.43 which reflects about a 62 percent increase over prior rates. According to annual reports filed by the utility to the SWRCB over recent years, customer complaints have been minimal. Also, system problems, including outages and mainline breaks, have been very infrequent.

Current production from the treatment plant is estimated at 7.3 million gallons per year (2016) with a peak daily system usage of approximately 60,000 gallons. The treatment plant uses two contact clarification pressure filters in two treatment trains for a total design capacity of 120 gallons per minute. Water quality test data shows excellent quality with total dissolved solids of a very low 104 milligrams per liter (mg/l), 52 mg/l hardness (as calcium carbonate) and no detection of total nitrates. Other test results were also very low or non-detected in comparison to standards.

## UTILITY REGULATION

The primary regulatory agencies that exert jurisdiction over the HCWC system operations and rates are the California PUC and SWRCB. The former agency only has jurisdiction over investor owned systems and purchasers whereas the latter regulates all potable water systems in the County (including both investor owned and public agency systems).



### **CALIFORNIA PUBLIC UTILITIES COMMISSION (PUC)**

The California PUC has jurisdiction over privately owned water utilities in the state including regulation of rates, financial practices and operating adequacy. PUC policies regarding the acquisition of water systems by regulated investor owned water companies, rate regulation and financial performance have to be taken into account when considering the potential fair market value of the HCWC system. Discussion of relevant PUC policies affecting the fair market value of this system is presented below. The PUC notes in its most recent March 2018 rate resolution that the HCWC has no outstanding compliance orders and meets all applicable drinking water standards.

### **STATE WATER RESOURCES CONTROL BOARD (SWRCB)**

The SWRCB has regulatory compliance authority over all water systems in the county, including those owned by both public agencies and investors (PUC regulated). The SWRCB enforces state waterworks standards (design and operations), operator competence, drinking water standards and many other policies to ensure the safety and potability of a public water system. The current regulatory status of the HCWC system was discussed with Ms. Mey Bunte, a representative of the SWRCB, in addition to obtaining selected regulatory reports. According to the SWRCB, the system operates well and produces a high-quality finished water that meets standards and customer demands.

### **COMPARABLE MARKET SALES**

SB 1268 required the PUC to recognize the fair market value paid for a qualifying utility (large Class A or B utility) up to RCNLD as the succeeding rate base (i.e. escalate the seller's rate base to equal the price paid). Prices paid exceeding RCNLD which would be recognized in rate base are even possible if economic advantages are demonstrated. Systems targeted for potential rate base escalation are those smaller systems having financing or regulatory problems where economies of scale or other efficiencies might be achieved

through acquisition by larger utilities. However, the legislation continued to authorize the PUC to have the power of disapproval over any sale not in the public interest.

In view of the small size and location of HCWC, it is considered that there are no potential large Class A water utilities which might acquire it. Typically, such acquisitions only occur where the small system is in close proximity to the buyer's larger regulated system, substantial potential growth exists or where several thousand connections are in the general regional area potentially to be acquired perhaps through multiple acquisitions. These market characteristics do not exist in the case of HCWC making a potential purchase by a Class A utility and associated rate base escalation approaching RCNLD speculative and improbable. However, Del Oro Water Company, a Class B utility would have the ability to escalate the rate base as a result of a sale paying more than the existing rate base and operating it together with its many other northern California small water systems. There are also no public agencies identified which potentially would acquire this system.

For the above reasons, and in view of the absence of comparable small system sales in recent years, this approach to value was not utilized in this appraisal.

### **CAPITALIZATION OF EARNINGS**

One of the marketing alternatives available to HCWC is to sell its system to a private regulated investor. Potentially, the HCWC system could be sold to either an individual as a sole proprietorship or an incorporated investor-owned water utility. An indication of the value of the HCWC system assets sold to a regulated investor can be developed through the capitalization of earnings approach.

The operations of a water utility in California including earnings (if not a mutual water company or in the possession of a public agency), are required to be regulated by the California PUC if charges are applied to water deliveries. The HCWC system, currently under PUC jurisdiction, would continue to be regulated by the PUC if the system were sold to a private investor. Under the

policies of the PUC, the earnings are designed to yield a fair rate of return on the capital invested by the owners of the utility. This invested capital is referred to as rate base.

#### **RELATIONSHIP BETWEEN RATE BASE AND CAPITALIZED EARNINGS VALUE**

The earnings allowed can be expected to be established at levels which will yield a rate of return on capital invested by the owners of the utility sufficient to attract capital considering other investment opportunities. Assuming that earnings are maintained by rate adjustments when necessary, then capitalization of these earnings (at a capitalization rate equal to the fair rate of return allowed by the PUC) would by definition result in a number equal to the rate base. This is demonstrated by the following example (with the specific figures in the example being for illustrative purposes only and assuming 100 percent equity):

Rate Base = \$150,000

Rate of Return allowed by PUC = 10%

Then the PUC will allow water rates sufficient to produce net revenues which will provide (after general and administrative costs, operating expenses, taxes and depreciation) an annual income of:

$0.10 \times \$150,000 = \$15,000$  per year

The amount which a purchaser would be willing to pay for a system which would produce a net income of \$15,000 per year, if the purchaser were willing to accept a 10 percent return on his investment, would be:

$\frac{\$15,000}{0.10} = \$150,000$

This is equivalent to the rate base.

It should be noted that although the rate base and the capitalized earnings value are the same numbers, conceptually they are different values.

To the extent that the PUC allows a fair rate of return on the rate base higher than a rate of return demanded by an investor considering other potential investments, or to the extent that growth pressures or other factors enhance the expectation of future earnings, the purchaser could be expected to be willing to pay a premium over the rate base. However, if not a Class A or B utility having the ability to escalate the rate base, the only way a small regulated buyer can pay more than rate base is through a stock acquisition retaining the rate base of the seller. Alternatively, if expected earnings in the estimation of the buyer are lower than required considering other potential investments, then the price paid by the buyer could be expected to be even a discount from the rate base.

#### **ESTIMATED RATE BASE**

The operations of an investor owned water utility in California including earnings are required to be regulated by the California PUC if charges are applied to water deliveries. The HCWC system is currently under PUC jurisdiction. Under the policies of the PUC, the earnings are designed to yield a fair rate of return on the capital invested in the facilities by the owners of the utility. This invested capital is referred to as rate base.

The rate base which may be expected to be allowed for facilities owned by an investor-owned utility by the PUC is normally made up of the following elements:

1. The historic capital costs of the facilities comprising the utility plant which remain in service;
2. A deduction for the accumulated depreciation applicable to the foregoing facilities computed in accordance with the policies of the PUC;
3. Deductions for that portion of the utility plant financed by means other than investment by the utility owner. These deductions include grants, contributions in aid of construction (on the basis of the depreciated value of the facilities represented by these contributions) and unreimbursed advances for construction remaining on the books at the time of computation of the rate base;

4. Deductions for any portions of the depreciated costs which represent an imprudent expenditure of funds, including money used for facilities not used or useful in supplying the water system demands or for over-design of the system;
5. Allowances for working cash and for materials and supplies;
6. An allowance for the given rate making unit's pro rata share of common plant (such as a utility's general offices) in the case of larger water companies owning multiple water systems.

Several of the above items, including working cash and common plant, although they would typically make up a part of the rate base, do not relate to the property being valued in this report.

#### **ESTIMATED EXISTING RATE BASE OF THE HCWC SYSTEM**

Theoretically, a qualified buyer (either a Class B utility defined as having in excess of 2,000 connections, or a Class A utility having over 10,000 connections) could request from the PUC a stepped up rate base based on a purchase price above the existing rate base in accordance with PUC Code Section 2719. This possibility is taken into account below.

In the case of HCWC, most of the utility infrastructure has been financed through a state grant which is not allowed to be added to the rate base. In the 2018 rate case, the rate base was determined to be only \$3,266.

#### **RATE OF RETURN AND PROJECTED EARNINGS**

As stated above, the PUC will authorize rates sufficient to generate earnings in order to attract investment and finance capital considering other market opportunities are competing for these same items. Earnings for a small 100 percent equity financed utility are measured as a rate of return to the utility investment overall as indicated by the rate base. The authorized return varies between utilities based on current economic conditions and a judgment of the shareholder's risk for a particular utility based on a variety of factors.



As indicated above, the rate base for the HCWC is minimal. Also, due to the small size and remote location of this system, it is considered improbable that a large Class A regulated purchaser could be found. However, it is estimated that a smaller regulated purchaser not having the ability to escalate the rate base might be located who would be a potential buyer. Also, it is known that DOWC, a class B utility, is interested in potentially acquiring the system. In the case of a Class B buyer, as indicated above, the sale price would become the succeeding rate base following sale.

For utility class D buyers, the current year targeted rate of return by the PUC in rate proceedings ranges from 10.56 to 11.56 percent (per PUC memorandum dated February 27, 2018). The average recent rate of return awarded to Class B utilities is reported to be 10.07 percent. It is considered that 11.5 percent and 10.1 percent are reasonable rates of return to calculate the capitalized earnings values potentially to be paid by these buyers.

A rate proceeding for HCWC has just been completed (W-5161, March 22, 2018). The projected net revenue by the PUC is \$10,368 based on operation as a Class D utility and rates established with a return on margin (or ROM, see below). The new 2018 rates will increase for an average customer by 61.6 percent. This significant rate increase and its yet unknown effect on water usage supports my decision to capitalize net income at the higher end of the rate of return range for Class D utilities. The rate proceeding projected a net income for HCWC in the amount of \$10,368. However, this projected amount was based on ROM with no allowance for depreciation. In the case of a sale to a Class B utility, the succeeding rate base would be established at the sale price. Consequently, a buyer would take into account the need to reduce this net income by estimated depreciation of the succeeding rate base. Even in the case of a Class D investor purchaser acquiring the stock of HCWC, a depreciation accounting would be made to provide for the return of the purchase investment even if this allowance is not accounted for in rates

#### **CAPITALIZED EARNINGS VALUE BASED ON RETURN TO RATE BASE**

As derived in this report, it is my opinion that the fair market value of this utility is \$80,000. As indicated above, it is anticipated that a smaller Class D buyer would require a rate of return on his investment of 11.5 percent. The

projected net income derived in the recent rate case, less depreciation for the buyer's investment and revised tax amounts to account for a depreciation deduction, amounts to \$8,570. Capitalization of this amount at a capitalization rate of 11.5 percent would indicate a potential sales price of approximately \$75,000.

For a lower required rate of capitalization of 10.1 percent, a Class B buyer could pay more for the system compared to a smaller buyer. Capitalizing the same projected net income as above amounts to approximately \$85,000. However, a review of projected expenses under ownership of a larger utility indicates that some of the operating expenses of the HCWC may be difficult to maintain at the same level. Therefore, it is believed that a Class B purchaser would pay no more than \$80,000 to better any offer from a potential small Class D purchaser .

#### **CAPITALIZED EARNINGS VALUE BASED ON RATE OF MARGIN**

For smaller systems having insufficient rate bases to generate adequate net incomes, the PUC policy is to set rates based on an alternative approach to establishing a net revenue by calculating a rate of margin (ROM) on operating costs (including operating costs, taxes other than income and depreciation on non-contributed plant). The ROM approach to establishing rates is not available to Class A or B utilities. Whichever approach (return to rate base or return on operating costs) results in the higher net income to a Class D owner, the PUC is mandated to utilize the higher approach to authorize rates. Based on the 2018 PUC rate resolution for the HCWC adopting a 23.87 percent ROM, the resulting prospective net income based on this approach indicates an amount of \$10,368 which, after accounting for depreciation, is what a return to the sale price would allow. However, the sales price paid by a Class B buyer would become the succeeding rate base which would also have to account for a depreciation allowance in assessing rate impacts.

#### **REPRODUCTION COST NEW LESS DEPRECIATION**

The reproduction cost new less depreciation (RCNLD) method of valuation, also known as the cost approach, is based on an estimate of the current cost of



construction for the physical facilities of the water system, less the estimated actual depreciation to account for the facilities being less than new. Additionally, separate amounts are added for the current market value of land, land rights, water rights, and the estimated current cost of intangible assets (such as organization costs).

As required by PUC policy for filing an application for any water system sale approval, an RCNLD analysis of the HCWC was performed. The total original cost utility plant in service for HCWC as of the date of value is reported to be \$953,365 (per 2017 PUC annual report). However, as indicated above, the source of most of this financing was a Prop. 50 grant in the amount of \$929,138 to install new treatment facilities, a 100,000 gallon reservoir and related plant. This new plant was completed in May 2015. Grant funded contributed plant is excluded from an RCNLD evaluation of any proposed PUC sale approval request. The remaining original utility cost represents pipeline and distribution facilities constructed in the 1960 original Rim Rock Subdivision plus system extensions and improvements installed from 1970 through 1983.

Attachment A presents the estimated RCNLD amount for the utility financed plant. As shown, the estimated RCNLD amount for the HCWC as of the date of value is approximately \$120,000. Detailed inventory records on selected associated plant items, such as distribution valves, services and meters, were not available to determine historic asset ages. In such cases, assumptions were made regarding sizes and ages of facilities. Further, a significant amount of system facilities appear to be near the end of their useful lives. Estimating remaining lives is very difficult when facilities are at this level of depreciation resulting in an uncertain RCNLD analysis. Regardless of these difficulties, it is regarded that the derived RCNLD value for HCWC is well above the opinion of value reached in this report.

### **OPINION OF VALUE**

In arriving at an opinion of value, I used or considered the traditional approaches to value: the earnings approach and the cost approach. Under the earnings approach, the prospective future stream of earnings was capitalized at

a rate consistent with the rate of return available on other comparable investments. I looked at both of these measures of value and took into account special circumstances concerning this system which might have an influence on value (including service area characteristics, service problems, system condition and design, general economic conditions and current earnings levels, status of regulatory proceedings, and ratepayer satisfaction with current service). On the basis of this information and my experience and knowledge, I then, by judgment, formed an opinion as to the fair market value.

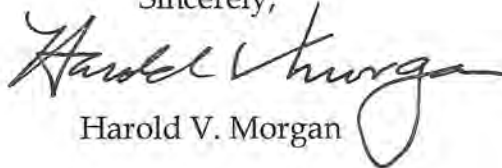
The approaches to value yield the following results:

Value indicated by Market Sales Approach	Not Determined
Value indicated by Capitalized Income Approach	\$80,000
Value indicated by RCNLD Approach	\$120,000

Correlation of the these approaches as presented above was made giving major weight to the capitalized earnings approach, typically relied on in appraisal practice as being one of the strongest evidences of value. However, the value indicated from the cost approach is very strong evidence to support the value derived from the earnings analysis.

Therefore, based on the above-described investigation, it my opinion that the fair market value of the water system facilities of the HCWC water system, including land and water rights, operating rights, going concern value, and water system materials and supplies as of December 31, 2017 is \$80,000. I will be pleased to answer any questions you might have regarding the above analysis.

Sincerely,



Harold V. Morgan

ATTACHMENT A

RCNLD ANALYSIS FOR HAT CREEK WATER SYSTEM

TABLE 1  
ESTIMATED RCNLD FOR HAT CREEK WATER SYSTEM

DESCRIPTION	SIZE	AMOUNT	UNIT	UNIT COS	RCN	YEAR CONST	AGE	INITIAL LIFE	REM LIFE	REVISED LIFE	REMAIN VALUE
Transite AC pipeline	3-inch	1233	feet	40	49320	1960	58	60	9	67	6625
Transite AC pipeline	4-inch	3593	feet	45	64170	1960	58	60	9	67	8620
PVC Schedule 40 pipeline	2-inch	1426	feet	35	49910	1983	35	60	25	60	20796
PVC Schedule 40 pipeline	3-inch	2096	feet	40	83840	1980	38	60	22	60	30741
PVC Schedule 40 pipeline	4-inch	900	feet	45	40500	1980	38	60	22	60	14850
PVC Schedule 40 pipeline	4-inch	1269	feet	45	57105	1970	48	60	12	60	11421
Distribution Valve	3-inch	1	number	250	250	1960	58	30	3	61	12
Distribution Valve	4-inch	3	number	375	1125	1960	58	30	3	61	55
Distribution Valve	4-inch	2	number	375	750	1970	48	30	4	52	58
Distribution Valve	3-inch	3	number	250	750	1980	38	30	5	43	87
Standpipe Hydrant	1.5-inch	4	number	700	2800	1980	38	60	22	60	1027
Service and Meter	5/8x3/4	27	number	1000	27000	1960	58	30	3	61	1328
Service and Meter	5/8x3/4	30	number	1000	30000	1980	38	30	5	43	3488
Service and Meter	1-inch	3	number	1250	3750	1980	38	30	5	43	436
Service and Meter	1.5-inch	1	number	1700	1700	1980	38	30	5	43	198
Service and Meter	2-inch	1	number	2200	2200	1980	38	30	5	43	256
Service and Meter	3-inch	1	number	2500	2500	1980	38	30	5	43	291
	Subtotal				417670						100289
	Indirects at 20%				83534						20058
	Totals				501204						120347

(a) Without detailed inventory information, sizes and years of construction for distribution valves, services and meters had to be estimated.  
(b) Obsolete materials such as transite AC pipeline would be replaced with PVC.

## **Exhibit E**

**Del Oro Water Company  
Hat Creek District  
Advice Letter No. 510**

**Proposed Summary of Earnings  
And Rate Base**

EXHIBIT E  
HAT CREEK WATER DISTRICT  
SUMMARY OF EARNINGS  
TEST YEAR 2019

	A	B	C
Line No	Hat Creek Water Company		
	Item	W-5161	DOWC
	Operating Revenues	3/22/2018	
1	460 Flat rates		
2	470 Metered rates	53,800	53,800
3	462 Private fire protection		
4	TOTAL REVENUE	53,800	53,800
5	Operating Expenses		
6	610 Purchased water	2,245	2,245
7	615 Purchased power	2,816	2,816
8	618 Other volume related	2,906	2,906
9	630 Employee labor	3,900	3,900
10	640 Materials	2,001	2,001
11	650 Contract work	3,551	3,551
12	660 Transportation expense	1,028	1,028
13	664 Other plant maintenance	2,348	2,348
14	670 Office salaries	1,455	1,455
15	671 Management salaries	4,989	4,989
16	674 Employee pension & benefits	1,900	1,900
17	676 Uncollectible	12	12
18	678 Office services & rentals	0	0
19	681 Office supplies & expense	2,489	2,489
20	682 Professional services	892	892
21	684 Insurance	2,646	2,646
22	688 Regulatory commission expense	131	131
23	689 General expenses	3,887	3,887
24	SUBTOTAL	39,195	39,195
25	403 Depreciation	0	2,664
26	408 Taxes other than income	208	595
27	409/10 Income taxes	4,029	3,283
28	Total Deductions	43,432	45,737
29	Net Revenue	10,368	8,063
30	Rate Base	3,266	80,000
31	Rate of Return	23.870%	10.08%

6,756,781	Gallons	2017
903,313	CF	
9,033	CCF	
Customer Number & Meter Sizes		
54	5/8"	
6	1"	
1	1.5"	
1	2"	
1	3"	
63		

**EXHIBIT E  
HAT CREEK DISTRICT  
RATE BASE**

**HAT CREEK DISTRICT  
SCHEDULE A-1c  
Account 101.2 - Water Plant in Service - Grant Funds**

Line No.	Acct No.	Title of Account (a)	Balance Beg of Year (b)	Plant Additions During year (c)	Plant (Retirements) During year (d)	Other Debits* or (Credits) (e)	Balance End of year (f)
1		<b>NON-DEPRECIABLE PLANT</b>					
2	301	Intangible Plant	381,638				\$ 381,638
3	303	Land	10,000				\$ 10,000
4		Total non-depreciable plant	\$ 391,638	\$ -	\$ -	\$ -	\$ 391,638
5							
6		<b>DEPRECIABLE PLANT</b>					
7	304	Structures	100,509				\$ 100,509
8	307	Wells					\$ -
9	311	Pumping Equipment	12,813				\$ 12,813
10	317	Other Water Source Plant					\$ -
11	320	Water Treatment Plant	67,376				\$ 67,376
12	330	Reservoirs, Tanks and Sandpipes	65,336				\$ 65,336
13	331	Water Mains	10,960				\$ 10,960
14	333	Services and Meter Installations	1,534				\$ 1,534
15	334	Meters	5,748				\$ 5,748
16	335	Hydrants					\$ -
17	339	Other Equipment	297,451				\$ 297,451
18	340	Office Furniture and Equipment					\$ -
19	341	Transportation Equipment					\$ -
20		Total depreciable plant	\$ 561,727	\$ -	\$ -	\$ -	\$ 561,727
21		<b>Total water plant in service</b>	\$ 953,365	\$ -	\$ -	\$ -	\$ 953,365

\* Debit or credit entries should be explained by footnotes or supplementary schedules

2,001	Utility Plant
3,266	Materials & Supplies
3,266	Working Cash
<u>(955,815)</u>	Grant/Depreciation
3,266	Rate Base per Resolution W-5161
<u>76,734</u>	Acquisition Adjustment
<b>80,000</b>	<b>Purchase Price per Appraisal</b>



## **Exhibit F**

**Del Oro Water Company  
Hat Creek District  
Advice Letter No. 510**

**Notice to Customers  
To Be Provided Under Separate Cover**

**Del Oro Water Company  
Hat Creek District**

**Service List for Advice Letter No. 510**

**California Public Utilities Commission**

Daniel Song  
Division of Water and Audits  
415-703-2691  
[water\\_division@cpuc.ca.gov](mailto:water_division@cpuc.ca.gov)

**California Public Utilities Commission**

Division of Ratepayer Advocates  
[dra\\_water\\_al@cpuc.ca.gov](mailto:dra_water_al@cpuc.ca.gov)

**Del Oro Water Company, Inc.**

[servicelist@delorowater.com](mailto:servicelist@delorowater.com)

**Larry Lees, Shasta County Administrative Officer**

1450 Court Street, Ste. 308A  
Redding, CA 96001-1673  
1-530-225-5561  
[llees@co.shasta.ca.us](mailto:llees@co.shasta.ca.us)

**Big Springs Mutual Water Co.**

P.O. Box 132  
Old Station, CA 96071  
[Hatcrk49@citilink.net](mailto:Hatcrk49@citilink.net)

**CDDW**

364 Knollcrest Dr., Suite 101  
Redding, CA 96002  
[dwpredning@waterboards.ca.gov](mailto:dwpredning@waterboards.ca.gov)

**Jack Hawks, Director**

CWA  
601 Van Ness Ave., Ste. 2047  
San Francisco, CA 94102  
[jhawks@calwaterassn.com](mailto:jhawks@calwaterassn.com)

## CERTIFICATE OF SERVICE

I certify that I have by mail this day served a true copy of Advice Letter No. 510 on all interested persons and organizations in these filings or their attorneys as shown on the attached list.

Dated: February 22, 2019, at Chico, California

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Lori L. Charlesworth

## NOTICE

Interested Persons and Organizations should notify the Water Division, Public Utilities Commission, 505 Van Ness Avenue, Room 4002 San Francisco, CA 94102, of any change of address to ensure that they continue to receive documents. You must indicate the Resolution number on the service list on which your name appears.